

EX PARTE

July 27, 2012

Ms. Marlene H. Dortch, Secretary Federal Communications Commission 445 12th Street, S.W. Washington, D.C. 20554

Re: In the Matter of Connect America Fund High-Cost Universal Service Support-Model Design and Data Inputs for Phase II of the Connect America Fund, WC Docket Nos. 10-90 and 05-337

Dear Ms. Dortch:

The National Association of State Utility Consumer Advocates ("NASUCA") files these additional comments regarding the above matter. This Ex Parte supplements NASUCA's initial comments filed on July 9, 2012 in this matter.¹

The cost benchmark should be set to induce carriers to participate in the CAF II model program.

The FCC should not adopt the American Cable Association's ("ACA") recommendation that the cost benchmark² should be set at the incremental average per unit ("ARPU") that a local exchange carrier ("LEC") will realize from extending their

¹ NASUCA as an organization, and NASUCA members the Maine Office of the Public Advocate, the New Jersey Division of Rate Counsel ("Rate Counsel") and The Utility Reform Network ("TURN") (collectively, "Consumer Advocates") filed initial comments.

² The cost benchmark is a/k/a the target benchmark or the low-end benchmark. The extremely high cost threshold is a/k/a the alternative technology benchmark or the high-end benchmark.

digital subscriber line ("DSL") networks to non-broadband customers.³ This recommendation is based on the fact that model does not determine the incremental cost of providing broadband service, given existing facilities. Instead, the model is estimating the total forward-looking cost of a network that can provide both narrow-band and broadband services. Thus the benchmark should reflect the average revenue from **both** voice and broadband customers.

Second, ACA assumes that 90 percent of the customers will be broadband customers. This assumption is based on the 90 percent number used in Cost Quest Associates Broadband Analysis Tool ("CQBAT"). ACA, however, is misinterpreting the CQBAT 90 percent number. It is not a broadband penetration assumption. Instead, it used to determine the number of Census households that the model will serve and where broadband services are available. That is, the model will build cable to and place drops and interface devices to 90 percent of the houses in each Census block. A 90 percent broadband penetration rates substantially the exceeds current national average penetration rates of 67 percent for households with any type of fixed broadband services and 38 percent for households with fixed broadband service greater than 3 MBPS downstream. Moreover, it must be noted that the current national average represent a long time period of adoption and do not reflect penetration rates that would exist after one to five years of service availability. Therefore, the broadband adoption rate used to determine the cost benchmark should be substantially below 90 percent.

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³ ACA Comments at 21.

⁴ Id., at 22.

⁵ Letter from Robert W. Quinn, AT&T to Chairman Julius Genachowski, FCC, July 29, 2011, July 29, 2011, WC Docket 10-90, ("ABC Plan"), Attachment 3, at 19.

⁶ Internet Access Services: Status as of June 30, 2011, FCC, Industry Analysis and Technology Division, June 2012.

Third, the ARPU associated with the broadband service does not match the costs estimated by the ABC Coalition's CQBAT model. Importantly, the CQBAT model does not include Internet transport costs, where Internet transport costs are the cost of using the services of Internet backbone carriers. For large peering carriers, Internet transport costs are zero. However, for small and medium sized carriers, Internet transport costs may be positive. Therefore, the ARPU should be reduced, when applicable, by the national average Internet transport cost.

Fourth, ACA recommends that additional revenue, such as special access services sold to wireless carriers, should be included in the cost benchmark. While the Consumer Advocates agree that these additional revenues would occur, estimating th0se revenues is highly speculative and would add substantial uncertainty to the investment decisions of participating carriers. Instead, the Consumer Advocates recommend again that the FCC adopt the principles stated in the State Joint Board members' plan that universal service payments should not allow a carrier to earn more than a just and reasonable rate of return. Thus, instead of engaging in the highly speculative venture of estimating addition revenues, the FCC would review the books and records of the carrier. If the additional revenues and the universal service funding increase the carrier's rate of return above a just and reasonable rate of return, the carrier would be required to return universal service funding such that its rate of return does not exceed that standard.

Instead of adopting the ACS recommendation, in order to fulfill the goal of universal broadband availability, the cost benchmark should be set to induce carriers to

⁷ It does not appear that these rates are required to be set at zero according to the FCC's bill and keep regime that was initiated by the Transformation Order.

⁸ ACS Comments, at 21.

participate in the program, yet without creating a universal service support windfall. Support should be sufficient but not excessive. Carriers will not participate if the revenues that they predict will result from new investment are below their anticipated costs. Therefore, the sum of revenues from customers plus universal service support must equal the total cost of service (recognizing that not all customers may choose to adopt the newly available broadband-based services). It must be realized, however, that total cost of providing service is not generated by the broadband network model. As noted above, the total cost, for non-peering carriers, includes Internet transport costs. Thus, to provide an opportunity to earn a fair rate of return, the cost benchmark should be set equal to the anticipated customer revenue minus non-network costs. Such a benchmark is similar to the methodology of the Commission's National Broadband Plan that attempted to determine support on the basis of a revenue gap. A cost benchmark that meets this criterion is probably closer to \$65¹⁰ than the ABC Coalition's proposed \$80.¹¹ If the cost benchmark is higher than this amount, carriers may be reluctant to participate. However, given the budget constraint, this lower cost benchmark would require a low extremely high-cost threshold, forcing a relatively high number of areas and customers into the Remote Area fund. Given that the Remote Area fund cannot possibly

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⁹ In the Matter of Connect America Fund, WC Docket No. 10-90, Notice of Inquiry and Notice of Proposed Rulemaking, FCC 10-58, released April 21, 2010, Appendix C: Omnibus Broadband Initiative, The Broadband Availability Gap.

¹⁰CenturyLink offers a bundle of phone and Internet services for \$64.95. http://www.centurylink.com/home/bundles/

¹¹ The ABC Coalition's \$80 proposal appears to be based on shape of the estimated cost curve, where \$80 is the inflection point where the "hockey stick" curve becomes vertical. While this point looks good on a graph, there is no public policy rationale for adopting that number. ABC Plan, at 20.

provide sufficient service for all of those customers, it is obvious that the entire fund is insufficient.¹²

The extremely high-cost threshold should not be used to determine the remote areas for rate-of-return carriers.

The Consumers Advocates agree with the Nebraska Rural Independent Companies ("NRIC") that the extremely high-cost threshold should not be used to determine the remote areas for rate-of-return carriers. 13 That threshold should not be used because it is determined relative to the Price-Cap carrier budget constraint. The rate-of-return carriers' support is not part of that budget constraint and therefore, using the Price-Cap carrier constraint to determine rate-of-return carrier support allocation is unreasonable. Second, the model inputs reflect the costs and bargaining power of the larger carriers that are part of the ABC Plan coalition. It is generally assumed that small carriers do not have the same bargaining power as the larger carriers, and, therefore, small rate-of-return carriers have higher equipment and facilities costs than the large carriers. This implies that even if the FCC wishes to use the ABC model to estimate rateof-return carrier costs, it must first make a bargaining power adjustment to increase the costs of these inputs. Third, the FCC has not determined how it intends to provide Connect America Fund II support to rate-of-return carriers. Decisions regarding rate-ofreturn carrier support in remote areas should be made in conjunction with the rate-ofreturn CAF II plan, and not as an add-on to the Price-cap carrier CAF II plan.

¹² It cannot be sufficient even if the service is satellite service because of the large number of consumers that would be forced into the remote area. Moreover, satellite service is an obvious inferior service and should not be imposed on large numbers of customers. In addition in remote areas, for public safety and economic development reasons, satellite service is not in the public interest. For example, satellite service does not meet the public safety needs of truckers, loggers, hikers, hunters, ranchers or other users of remote areas.

¹³ Nebraska Rural Independent Companies Comments, July 9, 2012.

Finally, the model can be used under specific guidelines to allocate the \$100 million Remote Area Fund between the Price-Cap carriers and the rate-of-return carriers. The guidelines are: (1) run the model for Price-Cap carries and determined the extremely high-cost threshold as discussed above; (2) count the number of lines served by Price-Cap carriers that are above the high-cost threshold; (3) run the model for rate-of-return carriers after adjusting inputs for bargaining power; (4) count the number of lines served by rate-of-return carriers after adjusting inputs for bargaining power that are above the extremely high-cost threshold; (4) allocate the \$100 million Remote Area Fund support based on the relative number of lines above the extremely high-cost threshold; and (5) add the rate-of-return allocation of the Remote Area Fund to the \$2 billion rate-of-return budget constraint.

Sincerely,

Charles A. Acquard
Charles A. Acquard
Executive Director
NASUCA
8380 Colesville Road, Suite 101
Silver Spring, MD 20910
Phone (301) 589-6313
Fax (301-589-6380
nasuca@nasuca.org